No. 70-28

In the Supreme Court of the United States

OCTOBER TERM, 1970

UNITED STATES OF AMERICA, PETITIONER

v.

EDNA GENDERS, WIFE OF, AND ALLEN H. GENDERS

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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INDEX

CITATIONS

407–052—70——1

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

The Solicitor General, on behalf of the United States of America, petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Fifth Circuit in this case.

OPINIONS BELOW

The district court did not render an opinion. The opinion of the court of appeals (Appendix A, *infra*, pp. 11–22) is reported at 427 F. 2d 279.

JURISDICTION

The judgment of the court of appeals was entered on May 25, 1970 (Appendix B, *infra*, p. 23). By order dated August 14, 1970, Mr. Justice Black extended the time for filing a petition for a writ of certiorari to and including October 22, 1970. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTION PRESENTED

Whether a shareholder-employee is entitled to a business bad debt deduction, arising out of his indemnification of corporate obligations, if, as the court below held, the undertaking was motivated to a significant degree by his business interest as an employee, or whether, as the United States contends, such a deduction is allowable only if the dominant motivation for the undertaking was his employee interest, rather than his nonbusiness interest as a stockholder.[1]

STATUTES AND REGULATIONS INVOLVED

The pertinent provisions of Section 166 of the Internal Revenue Code of 1954 and Section 1.166–5 of the Treasury Regulations on Income Tax (1954 Code) are set forth in Appendix C, *infra*, pp. 25–26.

STATEMENT

Respondent[2] owned 44 percent of the stock of the Kelly-Generes Construction Company, a corporation engaged in heavy construction work for various governmental authorities. The balance of the stock was owned by his son and two sons-in-law. Respondent was president of the corporation and, in that capacity, spent six to eight hours a week attending to its affairs,

[1] The government contended in the alternative below that, if a "significant" employee motivation is sufficient to justify business bad debt treatment, there was no such motivation in this case under any workable definition of that term. Although not separately discussed herein, that question is preserved in the event the Court grants certiorari.

[2] References to "respondent" are to Allen H. Generes. Edna Generes is a party hereto because joint income tax returns were filed for certain of the years in issue.

for which he was paid an annual salary of $12,000. His principal duties were to obtain bank financing for corporate activities and to secure performance and bid bonds on construction jobs undertaken by the corporation. In addition to serving as president of Kelly-Generes, respondent was employed full-time as president of a savings and loan association at a salary of $19,000 per year. (Appendix A, *infra*, p. 12.)

Late in 1958, respondent, both in his individual capacity and as president of Kelly-Generes, signed a "Blanket Indemnity Agreement" with Maryland Casualty Company under which Casualty agreed to furnish payment and performance bonds for Kelly-Generes, as required by the latter's government contracts. Respondent agreed therein to indemnify Casualty for any losses it suffered as surety up to $2,000,000. (Appendix A, *infra*, p. 13.)

In 1962, Casualty was required to complete performance on two Kelly-Generes contracts, and pursuant to the agreement, respondent indemnified Casualty for $162,104.57. Although subrogated to Casualty's rights as a creditor, he was unable to collect the amount of the indemnity from Kelly-Generes due to its subsequent bankruptcy. (Appendix A, *infra*, pp. 13–14.)

On his federal income tax return for 1962, respondent deducted the $162,104.57 against ordinary income as a business bad debt, and subsequently filed claims for refund for 1959–1961 based upon net operating loss carrybacks to those years in the amount of the unused

portion of the business bad debt deduction.[3] The Commissioner paid the carryback claim under the "quick" refund procedure prescribed in Section 6411 of the Internal Revenue Code. He later disallowed the net operating loss carrybacks on the ground that respondent's payment to Maryland Casualty gave rise to a deduction for a nonbusiness bad debt, which is defined in Section 166(d)(2) of the Internal Revenue Code as a debt other than—

> (A) * * * a debt created or acquired (as the case may be) in connection with a trade or business of the taxpayer; or
>
> (B) a debt the loss from the worthlessness of which is incurred in the taxpayer's trade or business.

Under Section 166(d)(1) such a deduction is treated as a short-term capital loss, and may not be carried back as a net operating loss. Respondent paid the tax in dispute and thereafter brought this suit for refund in the district court.[4] (Appendix A, *infra*, p. 14.)

The jury was asked (R. 189) to determine whether the signing of the blanket indemnity agreement by respondent was, as required by the Treasury Regulations as a prerequisite to business bad debt treatment, proximately related to his trade or business of being a Kelly-Generes employee. In this regard, the district court charged the jury, over the government's objection (R. 207), that (R. 195, 210, 211):

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[3] Although respondent was unable to collect an additional $158,814.49 in loans made by him directly to Kelly-Generes, he did not claim business bad debt treatment with respect to these loans (R. 115–116). ("R." references are to the printed record in the court of appeals.)

[4] That court's jurisdiction rested on 28 U.S.C. 1340.

> A debt is proximately related to the taxpayer's trade or business when its creation was *significantly motivated* by the taxpayer's trade or business, and it is not rendered a non-business debt merely because there was a non-qualifying motivation as well, even though the nonqualifying motivation was the primary one. [Emphasis added.]

The court refused the government's express request (R. 206–207) that the following instruction be given instead (Appendix B to the government's brief in the court of appeals, p. 41):

> You must, in short, determine whether Mr. Generes' dominant motivation in signing the indemnity agreement was to protect his salary and status as an employee or was to protect his investment in the Kelly-Generes Construction Co.
>
> * * * It is insufficient if the protection or insurance of his salary was only a significant secondary motivation for his signing the indemnity agreement. It must have been his *dominant* or most important reason for signing the indemnity agreement. [Emphasis added.]

The jury found (R. 213) that respondent's undertaking was proximately related to his trade or business of being an employee. This resulted in a verdict and a judgment for respondent. A divided court of appeals affirmed, holding that the jury had been properly instructed.

REASONS FOR GRANTING THE WRIT

1. The decision of the Fifth Circuit in this case, which follows a Second Circuit decision, is in conflict with the decision of the Court of Appeals for the

Seventh Circuit in *Niblock* v. *Commissioner*, 417 F. 2d 1185.

In *Weddle* v. *Commissioner*, 325 F. 2d 849, 851, the Second Circuit ruled that "it suffices for deduction [as a business bad debt] that the creation of the debt should have been significantly motivated by the taxpayer's trade or business, even though there was a non-qualifying motivation as well," and specifically rejected "as an erroneous view of the law" the contention that a taxpayer must prove that his primary motivation was to protect his trade or business of corporate employment in order to be entitled to a business bad debt deduction. In like manner, the court below refused (Appendix A, *infra*, pp. 11–21) to find error in the district court's charge to the jury that a significant employee motivation is sufficient to justify business bad debt treatment, even though the dominant motivation for the taxpayer's undertaking was his nonbusiness interest as an investor. In *Niblock*, on the other hand, the Seventh Circuit held (417 F. 2d at 1187) that, to obtain business bad debt treatment, a taxpayer "must prove that his corporate employment furnished the dominant and primary motivation" for his undertaking, stating, "We disagree with the significant motivation factor test that was applied by the majority in *Weddle* v. *Commissioner* * * *."[5]

[5] A third test has been proposed by Judge Stahl in a separate opinion (dissenting from the majority on another issue) in *Stratmore* v. *United States*, 420 F. 2d 461 (C.A. 3), certiorari denied, 398 U.S. 951, where the majority found it unnecessary to decide the dominant-significant question. His test (420 F. 2d at 469) would require the taxpayer to pro-

2. The Fifth and Second Circuits have incorrectly construed the applicable statute. The decision of the Seventh Circuit is correct.

Section 166 (a) and (d) of the Internal Revenue Code (Appendix C, *infra,* p. 25) provides that an individual taxpayer may deduct a bad debt against ordinary income only if the debt is created or acquired in connection with, or the loss therefrom is incurred in, the taxpayer's trade or business. Otherwise, the deduction is for a nonbusiness bad debt, deductible only as a short term capital loss. The problem here arises where a taxpayer bears a dual relationship—as shareholder and also as employee—to the corporation whose default gives rise to a bad debt loss. While his employee status constitutes a "trade or business," so that a loss resulting from a loan bearing the required degree of relationship to such status is deductible in full (*Trent* v. *Commissioner,* 291 F. 2d 669 (C.A. 2)), his shareholder status is not a "trade or business." Losses on loans made to advance a taxpayer's status as an equity owner accordingly are deductible only as nonbusiness bad debts. *Whipple* v. *Commissioner,* 373 U.S. 193. See also *Putnam* v. *Commissioner,* 352 U.S. 82.

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duce evidence "negating the possibility that investment considerations were so important that the transaction would have been undertaken even had the business considerations been entirely absent." While Judge Stahl refers to this as the "significant test," it would, in some instances, be more stringent than the dominant motivation test adopted by the Seventh Circuit. It would require nonbusiness treatment where, even though the employment status was the dominant factor, the investment interest was itself strong enough to have motivated the transaction.

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Until this Court's decision in *Whipple* v. *Commissioner, supra,* shareholders in closely held corporations sought to obtain business bad debt deductions resulting from their corporations' reverses on the ground that the loans had been made in the course of a business of organizing, operating and financing corporations. After that prospect of ordinary loss deductibility was severely limited by the Court in *Whipple,* stockholders have attempted to obtain the result there denied them on the theory that their loans or guarantees were motivated by a desire to protect their salaried position with their corporations. But, Mr. Justice White, speaking for the Court in *Whipple,* stated his understanding that this theory would not offer an easy route to business bad debt losses. He found on the facts in *Whipple* (373 U.S. at 204) that "there is no proof (*which might be difficult to furnish where the taxpayer is the sole or dominant stockholder*) that the loan was necessary to keep his job or was otherwise proximately related to maintaining his trade or business as an employee" (emphasis added).

The result below will, contrary to the principles announced in *Whipple,* permit easy access to business bad debt benefits for many corporate investors and circumvention of the holding in *Whipple* itself. See *Weddle* v. *Commissioner, supra,* pp. 852–853 (Lumbard, J., concurring). It substantially removes the difficulty which this Court thought a sole or dominant shareholder would have in establishing entitlement to an ordinary deduction. As the instant case itself illustrates (Appendix A, *infra,* pp. 18–19), adop-

tion of the significant motivation test[6] opens the possibility that a shareholder-employee will be able to obtain such treatment merely by introducing testimonial evidence that his undertaking was motivated in some degree by a desire to protect his job and salary.[7]

3. The proper treatment of deductions for bad debts arising from loans, guarantees or indemnities by shareholder-employees is a frequent subject of contention between the Commissioner of Internal Revenue and taxpayers. The Internal Revenue Service has advised us that there are presently pending at the appellate conference level of the Service 179 cases, involving more than $4,000,000 of tax, in which shareholder-employees are claiming business bad debt deductions on the ground that the debts were incurred

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[6] In approving this test, the Second and Fifth Circuits relied principally on Section 1.166–5 of the Treasury Regulations (Appendix C, *infra*, pp. 25–26), which provides that if a loss resulting from the worthlessness of a debt bears a "proximate" relationship to the taxpayer's trade or business, it may be deducted as a business bad debt loss. The use of the word "proximate" does not justify the result reached below. While as the above courts noted, a secondary cause may be viewed as "proximate" in the tort law, there is no reason why tort law concepts should control for federal tax purposes. That "proximate" is susceptible of another meaning is apparent from Black's Law Dictionary (4th ed.), which defines the term (p. 1391) as the "closest in causal connection," a phrase clearly indicating predominance.

[7] Here the jury believed that respondent was "significantly" motivated by his interest as an employee to expose himself to potential liability of $2,000,000, in order to protect a part-time job paying $12,000 a year. On the other hand, the record shows that respondent paid about $38,900 for his stock in Kelly-Generes (R. 84) and that, at the time the corporation went bankrupt, it was indebted to respondent on direct loans for $158,814.49 (R. 115–116).

in the trade or business of being a corporate employee. Many more cases are certain to arise because it is common for shareholder-employees, particularly in closely held corporations, to advance funds to, or guarantee the debts of, their corporations. The conflict in the circuits leaves the Commissioner and taxpayers uncertain of the standard to be applied. Review by this Court is therefore necessary to allow evenhanded treatment of similarly situated taxpayers.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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OCTOBER 1970.

APPENDIX A

In the United States Court of Appeals for the Fifth Circuit

No. 25713

UNITED STATES OF AMERICA, APPELLANT

v.

EDNA GENERES, WIFE OF, AND ALLEN H. GENERES, APPELLEES

Appeal from the United States District Court for the Eastern District of Louisiana

(May 25, 1970)

Before AINSWORTH and SIMPSON, *Circuit Judges,* and SINGLETON, *District Judge.*

AINSWORTH, *Circuit Judge:* By this appeal the United States brings here for review a jury verdict and judgment below for the taxpayer [1] in an income tax refund suit. Taxpayer, in the early 1940's, entered into a partnership engaged in the construction business in New Orleans, Louisiana, with his son-in-law, William F. Kelly, who had already established the business. Taxpayer and Mr. Kelly were equal partners in this operation.

In 1954, the partnership was incorporated as Kelly-Generes Construction Company, Inc., which was engaged primarily in heavy construction work for vari-

[1] Throughout this opinion "taxpayer" will be used in the singular to refer to the husband, Allen H. Generes, since his wife is a party only because joint returns were filed for two of the taxable years here involved.

ous federal, state, city and public authorities. The corporation was essentially a closed family corporation with taxpayer and Mr. Kelly each owning 44 percent of the corporate stock. The remaining 12 percent of the stock was divided between another son-in-law of taxpayer, Mr. Louis Treuting, and taxpayer's son, Allen H. Generes, Jr.

Taxpayer was president of the corporation and in that capacity spent only approximately six to eight hours per week attending to the affairs of the corporation. His principal duties as president of Kelly-Generes Construction Company, Inc. were to obtain bank financing for corporate activities and to secure performance and bid bonds on construction jobs undertaken by the company. In his individual capacity, taxpayer endorsed loans made to the corporation by various banks in New Orleans for the purpose of purchasing construction machinery and other equipment. In addition, taxpayer from time to time personally advanced funds to the corporation. Taxpayer, as president of the corporation, received a salary of $12,000 per year and Mr. Kelly, as vice-president and the one in charge of the day-to-day operations of the corporation, received a salary of $15,000 per year.

During all the years in question, taxpayer was the president of Central Savings and Loan Association in New Orleans of which he was the founder. This was a full-time job for which he received a salary in the amount of $19,000 per year. In addition, taxpayer had other sources of income; his federal tax returns for the years 1959 through 1962 indicate an average income of approximately $40,000 a year. Taxpayer, during the years in question, maintained bank accounts ranging in total amount from $30,000 to $55,000.

The construction contracts undertaken by the corporation generally required performance and payment bonds, the greatest number of which were obtained from the Maryland Casualty Company. Taxpayer was required to sign separate indemnity agreements with Maryland Casualty Company for each bond issued by that company for a job being performed by Kelly-Generes Construction Company, Inc. These indemnity agreements provided that taxpayer agreed to hold Maryland Casualty Company harmless from any losses suffered by reason of any defaults by the corporation which would require the surety company to perform or pay under its bonds.

Subsequently, in December of 1958, it was decided that it would be advisable for taxpayer to execute a blanket indemnity agreement in lieu of signing a separate indemnity agreement for each construction job. Thus, on December 3, 1958, an instrument entitled "Blanket Indemnity Agreement" with Maryland Casualty Company was signed by the corporation as applicant, through taxpayer its president, and in addition was signed individually by taxpayer and William Kelly as indemnitors. Under this agreement, taxpayer agreed to hold harmless the Maryland Casualty Company from any loss sustained as a result of its bonding the construction jobs of Kelly-Generes. At the same time, Maryland Casualty Company agreed to increase the surety credit of Kelly-Generes from approximately $1,000,000 to $1,500,000 for any one job and to a total credit line of $2,000,000 inclusive of all jobs bonded by them.

In 1962, Kelly-Generes underbid on two important projects and defaulted in the performance of its contracts. As a result, Maryland Casualty Company was forced to complete performance. Subsequently, Maryland Casualty Company sought enforcement of the

indemnity agreement of December 3, 1958 against taxpayer, and Mr. Kelly, and as a result the taxpayer, in 1962, was forced to pay $162,104.57 to Maryland Casualty Company. Kelly-Generes eventually went into receivership and taxpayer was unable to collect the above amount from the company as a subrogated creditor.

On the federal income tax return for 1962, taxpayer deducted the amount of the payment to Maryland Casualty Company as a business bad debt and subsequently filed claims for refund for the years 1959, 1960 and 1961 by virtue of a net operating loss carryback to those years arising from the unused portion of the 1962 business bad debt deduction. The Internal Revenue Service paid the claim upon the filing by taxpayer of the tentative carryback claim. However, the Internal Revenue Service later disallowed the net operating loss carryback on the ground that the payment by taxpayer to Maryland Casualty Company did not give rise to a business bad debt deduction.[2] Accordingly, assessments in the aggregate amount of $43,851.46 plus statutory interest were made against taxpayer on May 28, 1965. Payment of these assessments was received by the Internal Revenue Service on June 2, 1965, and, on June 8, 1965, taxpayer filed claims for refund of the amount previously paid. These were denied by the Commissioner and the suit below was timely filed thereafter.

Trial was before a jury. Both parties unsuccessfully moved for directed verdicts at the close of all the evi-

[2] If the bad debt in question could be classified as a business bad debt under 26 U.S.C. § 166(a)(1), the net operating loss carryback would be proper under the provisions of 26 U.S.C. § 172. If, however, the bad debt was of a nonbusiness nature as defined by 26 U.S.C. § 166(d), the taxpayer could not avail himself of the net operating loss carryback. 26 U.S.C. § 172(d)(4).

dence. Upon submission by special issues the jury returned a verdict under which the taxpayer was entitled to recover the amount in suit. The Government then moved for judgment n.o.v. and alternatively for a new trial. These motions were denied, judgment was entered in accordance with the verdict and this appeal followed. We affirm.

The facts recited above are as set forth in the Government's brief and are not disputed by taxpayer. The sole question presented is whether the taxpayer's loss gave rise to business bad debts within the meaning of 26 U.S.C. § 166.[3] In order to answer that question, it is necessary to determine whether the taxpayer's endorsement was motivated out of a desire to protect his trade or business, i.e., that of being president of the Kelly-Generes Construction Company. See *Kelly*

[3] The pertinent provisions of the statute are:

"§ 166. Bad debts

"(a) General rule.—

"(1) Wholly worthless debts.—There shall be allowed as a deduction any debt which becomes worthless within the taxable year.

* * * * *

"(d) Nonbusiness debts.—

"(1) General rules.—In the case of a taxpayer other than a corporation—

"(A) subsections (a) * * * shall not apply to any nonbusiness debt; and

"(B) where any nonbusiness debt becomes worthless within the taxable year, the loss resulting therefrom shall be considered a loss from the sale or exchange, during the taxable year, of a capital asset held for not more than 6 months.

"(2) Nonbusiness debt defined.—For purposes of paragraph (1), the terms 'nonbusiness debt' means a debt other than—

"(A) a debt created or acquired (as the case may be) in connection with a trade or business of the taxpayer; or

"(B) a debt the loss from the worthlessness of which is incurred in the taxpayer's trade or business."

v. *Patterson*, 5 Cir., 1964, 331 F. 2d 753; *Trent* v. *C.I.R.*, 2 Cir., 1961, 291 F. 2d 669.

Treas. Reg. § 1.166–5(b), 26 C.F.R. § 1.166–5(b), provides that the debt is deductible as a business bad debt only if "the relation which the loss resulting from the debt's becoming worthless bears to the trade or business of the taxpayer" is "*proximate.*" (Emphasis added.)

The Supreme Court indicated its approval of the "proximate relationship" test in *Whipple* v. *C.I.R.*, 373 U.S. 193, 83 S. Ct. 1168 (1963). In vacating and remanding *Whipple* to the Tax Court for a determination of whether a taxpayer's loan was made in his business of being a landlord, the Court noted:

> Moreover, there is no proof (which might be difficult to furnish where the taxpayer is the sole or dominant stockholder) that the loan was necessary to keep his job *or was otherwise proximately related* to maintaining his trade or business as an employee.

373 U.S. at 204, 83 S. Ct. at 1175. (Emphasis added.)

The District Court's sole interrogatory to the jury, answered in the affirmative, was phrased in terms of proximate relationship. The jury was asked:

> Do you find from a preponderance of the evidence that the signing of the blanket indemnity agreement by Mr. Generes was proximately related to his trade or business of being an employee of the Kelly-Generes Construction Company?

The Court instructed the jury that

> A debt is proximately related to the taxpayer's trade or business when its creation was significantly motivated by the taxpayer's trade or business, and it is not rendered a non-business debt merely because there was a non-

> qualifying motivation as well, even though the non-qualifying motivation was the primary one.

The Government urges that "dominant motivation" and not "significant motivation" was the appropriate test for determining the proximate relationship of the debt to the taxpayer's business and that the District Judge's charge to the jury was therefore erroneous. Neither the Supreme Court nor this Court has ruled on the precise question. However, the above-quoted language of the Supreme Court in *Whipple, supra,* which impliedly requires proof only that a loan be "proximately related" to the maintenance of a taxpayer's trade in order that a deduction be allowed, precludes the imposition of dominant motivation proof on the taxpayer. We are impressed with the majority holding in the Second Circuit decision in *Weddle* v. *C.I.R.,* 1963, 325 F. 2d 849, and its analogy between proximate cause and significant motivation.[4]

The Court in *Weddle* in disavowing the "primary" motivation test as an erroneous view of law, said:

> That is not what is said either by the statute or by the Regulations, which the Supreme Court inferentially approved in *Whipple* v. *C.I.R.,* 373 U.S. 193, 204, 83 S. Ct. 1168, 10 L. Ed. 2d 288 (1963). In the law of torts, where the notion of "proximate" causation is most frequently encountered, a cause contributing to a harm may be found "proximate" despite the fact that it might have been "secondary" to another contributing cause. See 2 Harper & James, The Law of Torts, §§ 20.2 and 20.3; American Law Institute, Restatement, Torts, §§ 432(2), 433, 439, 875, 879 (1939); Restatement

[4] The Government relies on a concurring opinion in *Weddle* which rejects the majority's "significant motivation" test and suggests as the proper criteria a "primary and dominant motivation."

> Second, Torts § 443A at 54 (Tent. Draft No. 7, 1962), § 442B at 29 (Tent. Draft No. 9, 1963). So here, particularly in view of the back-handed wording of § 166, it suffices for deduction that the creation of the debt should have been significantly motivated by the taxpayer's trade or business, even though there was a non-qualifying motivation as well.

325 F. 2d at 851.

We find no error in the District Court's instruction relative to the significant motivation of taxpayer in determining the proximate relation of a debt to his trade or business.

Therefore, if the evidence was such that the jury could have reasonably concluded that the taxpayer's endorsement was motivated by a desire to preserve his business of being a corporate employee the jury could have properly determined that the bad debt was proximately connected with the taxpayer's trade or business. Taxpayer repeatedly testified that he signed the agreement in order to protect his job and his salary as an officer of Kelly-Generes.[5] While admittedly much of the testimony was self-serving, the credibility and sincerity of taxpayer, the assessment of which is undisputably a jury function, were decided

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[5] The following cross-examination of Mr. Generes is pertinent:

"Q. Let me ask you what motivated you to endorse or sign those notes on behalf of the corporation?

"A. The corporation was paying me $12,000 a year. I had $38,000 in it, and I figured in three years' time I would get my money out. (App. 107)

* * * * *

"Q. I believe you also stated you were interested in your salary because, if you did not sign the indemnity agreement, the Maryland Casualty Company wouldn't execute the bonds and Kelly-Generes Construction Company couldn't get con-

in his favor.[6] Moreover, there was uncontradicted testimony of witnesses other than taxpayer from which

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tracts and, therefore, would go out of business, and you would lose your job; is that right?

"A. That is perfectly correct. (App. 118)

"Q. Is that the relationship between your signing of the indemnity agreement and your job?

"A. The reason I signed that indemnity agreement was to protect my job.

"Q. Through protecting your investment, through protecting Kelly-Generes Construction Company?

"A. The investment was very small, only $38,000, and I figured that if I signed this bond—I get $12,000 a year, in three years' time I would be practically paid out of my investment. * * *

"Q. At the time you signed it, did you give consideration to the fact that you were protecting your job and salary at the time you signed it?

"A. That's the reason I signed it. (App. 119)

"Q. To protect your job and salary?

"A. That's the reason I signed it.

"Q. Did you give any thought at all to your investment in the corporation?

"A. No, I never once gave it a thought. * * * I never thought about dividends because we were growing, and I signed the indemnity bond for the purpose of protecting my salary, and that is what I had in mind. (App. 120) * * * To tell you the truth about it * * * I never gave that a thought. I never gave my investment a thought. That $1,000 a month I was getting and trying, as I said, to build up an estate for my children." (App. 122)

[6] In *United States* v. *Worrell*, 5 Cir., 1968, 398 F. 2d 427, this Court reversed and remanded a decision in favor of taxpayer under circumstances somewhat similar to those here. At issue in *Worrell*, as here, was taxpayer's motivation in signing as an indemnitor of the corporation's surety creditor. However, one essential difference between *Worrell* and the present case exists: *Worrell* was tried to the Court entirely on stipulations and documentary evidence; there was no oral testimony and "no word from Mr. Worrell or anyone else as to what his motive was in signing these indemnity contracts." 398 F. 2d at 428.

the jury could have inferred that taxpayer's motivation in endorsing the agreement stemmed from his desire to protect his job and consequently his salary. The record shows that no performance bonds would have been issued to Kelly-Generes without the personal endorsement of Mr. Generes. Without the bonds the corporation would have gone out of business. The corporation was a closed corporation, privately held and no stock was available to the general public. At no time did the corporation pay dividends to its shareholders.

The ultimate question, therefore, is whether the evidence formed a sufficient basis to justify the Trial Judge's submission of the case to the jury. The applicable standard is that expressed in our recent en banc decision, *Boeing Company* v. *Shipman*, 5 Cir., 1969, 411 F. 2d 365, 374–375:

> On motions for directed verdict and for judgment notwithstanding the verdict the Court should consider all of the evidence—not just that evidence which supports the non-mover's case—but in the light and with all reasonable inferences most favorable to the party opposed to the motion. If the facts and inferences point so strongly and overwhelmingly in favor of one party that the Court believes that reasonable men could not arrive at a contrary verdict, granting of the motions is proper. On the other hand, if there is substantial evidence opposed to the motions, that is, evidence of such quality and weight that reasonable and fair-minded men in the exercise of impartial judgment might reach different conclusions, the motions should be denied, and the case submitted to the jury. A mere scintilla of evidence is insufficient to present a question for the jury. The motions for directed verdict and judgment n.o.v. should not be decided by which side has the better of the case, nor should they be granted only when

> there is a complete absence of probative facts to support a jury verdict. There must be a conflict in substantial evidence to create a jury question. However, it is the function of the jury as the traditional finder of the facts, and not the Court, to weigh conflicting evidence and inferences, and determine the credibility of witnesses. (Footnote omitted.)

Under the standards of *Boeing* we hold that the District Court properly denied the motions of the Government for judgment n.o.v. and for a new trial.

Affirmed.

SIMPSON, *Circuit Judge,* Dissenting: I respectfully dissent.

I believe that the only test that will inject sufficient certainty into the interpretation of Title 26, U.S.C. Section 166 is the *dominant and primary motivation test* articulated by Chief Judge Lombard in his concurring opinion in *Weddle* v. *Commissioner of Internal Revenue,* 2 Cir., 1963, 325 F. 2d 849, 851. The Seventh Circuit recently adopted this standard in *Niblock* v. *Commissioner of Internal Revenue,* 7 Cir., 1969, 417 F. 2d 1185.

The bare self-serving statements of Taxpayer were the sole evidence offered by him as to his motivation. If the dominant motivation criterion had been applied, I do not think these statements would have been sufficient under *Boeing Company* v. *Shipman* standards of proof [1] to take the case to the jury in the face of the clear proof that Generes and Kelly were required to sign the endorsement in order for the corporation to engage in the construction business. This problem of proof was prophetically forecast by

[1] The *Boeing Company* v. *Shipman,* 5 Cir. 1969, 411 F. 2d 365, 374, 375.

Whipple v. *Commissioner*, 373 U.S. 193, 204, 83 S. Ct. 1168, 10 L. Ed. 2d 288, 295:

> Moreover, there is no proof (*which might be difficult to furnish where the taxpayer is the sole or dominant stockholder*) that the loan was necessary to keep his job or was otherwise proximately related to maintaining his trade or business as an employee. (Emphasis supplied.)

On this basis, I would reverse the judgment below and remand with directions to the trial court to enter judgment N.O.V. in favor of the United States.

APPENDIX B

In the United States Court of Appeals for the Fifth Circuit

October Term, 1967

No. 25713

D.C. Docket No. CA 16156–C

UNITED STATES OF AMERICA, APPELLANT

v.

EDNA GENERES, WIFE OF, AND ALLEN H. GENERES,

APPELLEES

Appeal from the United States District Court for the Eastern District of Louisiana

Before AINSWORTH and SIMPSON, *Circuit Judges,* and SINGLETON, *District Judge.*

JUDGMENT

This cause came on to be heard on the transcript of the record from the United States District Court for the Eastern District of Louisiana, and was argued by counsel;

On consideration whereof, It is now here ordered and adjudged by this Court that the judgment of the said District Court in this cause be, and the same is hereby, affirmed.

It is further ordered, That appellant pay to appellees, the costs to be taxed by the Clerk of this Court.

SIMPSON, *Circuit Judge,* Dissenting:

"Per AINSWORTH, C. J."

May 25, 1970.

APPENDIX C

Internal Revenue Code of 1954 (26 U.S.C.):

SEC. 166. BAD DEBTS.

(a) *General Rule.*—

(1) *Wholly worthless debts.*—There shall be allowed as a deduction any debt which becomes worthless within the taxable year.

* * * * *

(d) *Nonbusiness Debts.*—

(1) *General rule.*—In the case of a taxpayer other than a corporation—

(A) subsections (a) and (c) shall not apply to any nonbusiness debt; and

(B) where any nonbusiness debt becomes worthless within the taxable year, the loss resulting therefrom shall be considered a loss from the sale or exchange, during the taxable year, of a capital asset held for not more than 6 months.

(2) *Nonbusiness debt defined.*—For purposes of paragraph (1), the term "nonbusiness debt" means a debt other than—

(A) [as amended by Sec. 8, Technical Amendments Act of 1958, P.L. 85–866, 72 Stat. 1606] a debt created or acquired (as the case may be) in connection with a trade or business of the taxpayer; or

(B) a debt the loss from the worthlessness of which is incurred in the taxpayer's trade or business.

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Treasury Regulatons on Income Tax (26 C.F.R.):

§ 1.166–5 *Nonbusiness debts.*

* * * * *

(b) *Nonbusiness debt defined.* For purposes of section 166 and this section, a nonbusiness debt is any debt other than—

(1) A debt which is created, or acquired, in the course of a trade or business of the taxpayer, determined without regard to the relationship of the debt to a trade or business of the taxpayer at the time when the debt becomes worthless; or

(2) A debt the loss from the worthlessness of which is incurred in the taxpayer's trade or business.

The question whether a debt is a nonbusiness debt is a question of fact in each particular case. The determination of whether the loss on a debt's becoming worthless has been incurred in a trade or business of the taxpayer shall, for this purpose, be made in substantially the same manner for determining whether a loss has been incurred in a trade or business for purposes of section 165(c)(1). For purposes of subparagraph (2) of this paragraph, the character of the debt is to be determined by the relation which the loss resulting from the debt's becoming worthless bears to the trade or business of the taxpayer. If that relation is a proximate one in the conduct of the trade or business in which the taxpayer is engaged at the time the debt becomes worthless, the debt comes within the exception provided by that subparagraph. The use to which the borrowed funds are put by the debtor is of no consequence in making a determination under this paragraph. For purposes of section 166 and this section, a nonbusiness debt does not include a debt described in section 165(g)(2)(C). See § 1.165–5, relating to losses on worthless securities.

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U.S. GOVERNMENT PRINTING OFFICE: 1970